

Internal Revenue Service

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Person To Contact:

Telephone Number:

Refer Reply To:

CC:PSI:B02

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Date:

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Legend

X =

State =

Properties =

D1 =

Year =

a =

x =

y =

Dear _____ :

This responds to a letter dated September 30, 2009, and subsequent correspondence, submitted on behalf of X by X's authorized representative, requesting a ruling that receipts from its parking facility business are not passive investment income within the meaning of § 1362(d)(3)(C)(i) of the Internal Revenue Code.

FACTS

The information submitted states that X is incorporated in State. X elected to be treated as an S corporation effective D1. X has accumulated earnings and profits.

X owns, operates, manages, and leases commercial real estate consisting of parking facilities (the Properties) among its other real estate businesses. X represents that it owns some of the Properties through qualified subchapter S subsidiaries and the others through partnerships with a third party. X manages the partnerships and the Properties they hold for a management fee paid by the partnerships.

X has a employees who spend time performing work related to the Properties. X has also made strategic use of a third-party national parking management company to provide labor and field management at X's direction. Through its staff, as well as through the management company, X provides various services to the Properties in its parking facility business. These services include accounting and bookkeeping; internal auditing; billing and collections; daily property inspection; common area maintenance; janitorial services; landscaping; maintenance and repair of building structural components and systems (plumbing, electrical, and mechanical); elevator maintenance and repair; provision of utilities; pest control; and provision of security services through a third-party. In addition, X handles the usual leasing and administrative functions involved in leasing portions of its parking facilities for use by other businesses.

For Year, X received \$x in receipts and X paid or incurred \$y expenses (other than depreciation) with respect to the Properties.

LAW AND ANALYSIS

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(d)(3)(A) provides that an election under § 1362(a) shall be terminated

whenever the corporation has accumulated earnings and profits at the close of each of 3 consecutive taxable years, and has gross receipts for each of such taxable years more than 25 percent of which are passive investment income. Any termination under this paragraph shall be effective on and after the first day of the first taxable year beginning after the third consecutive taxable year referred to above.

Section 1362(d)(3)(C)(i) provides that except as otherwise provided, the term “passive investment income” means gross receipts derived from royalties, rents, dividends, interest, annuities, and sales or exchanges of stock or securities.

Section 1.1362-2(c)(5)(ii)(B)(2) of the Income Tax Regulations provides that “rents” does not include rents derived in the active trade or business of renting property. Rents received by a corporation are derived in an active trade or business of renting property only if, based on all the facts and circumstances, the corporation provides significant services or incurs substantial costs in the rental business. Generally, significant services are not rendered and substantial costs are not incurred in connection with net leases. Whether significant services are performed or substantial costs are incurred in the rental business is determined based upon all the facts and circumstances including, but not limited to, the number of persons employed to provide the services and the types and amounts of costs and expenses incurred (other than depreciation).

CONCLUSION

Based solely on the facts and the representations submitted we conclude that the receipts that X derives from the Properties are not passive investment income as described in § 1362(d)(3)(C)(i).

Except as specifically set forth above, we express no opinion as to the federal tax consequences of the transaction described above under any other provision of the Code. Specifically, we express no opinion on whether X is a small business corporation eligible to make an S election. Further, the passive investment income rules of § 1362 are completely independent of the passive activity rules of section § 469; unless an exception under § 469 applies, the rental activity remains passive for purposes of § 469.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to X's authorized representative.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes